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SUBJECT: ETHIOPIA: INVESTMENT CLIMATE STATEMENT 2007

REF: STATE 178303

¶1. Begin Ethiopia's 2007 Investment Climate Statement:

OPENNESS TO FOREIGN INVESTMENT

There are few changes since last year's Investment Climate Statement report. The 2005/2006 highlights include:

-- A new proclamation governing trademark registration and protection was issued in July 2006

-- Despite relative stability and security for investors, sporadic political, religious and ethnic violence continued in some parts of the country, including the capital.

-- A recently published UN Investment Guide to Ethiopia indicated that, according to the private sector, routine bureaucratic corruption is virtually non-existent in Ethiopia. Transparency International recorded a decline in Ethiopia's ranking from 114th out of 145 countries rated in 2004 to 130th out of 160 countries rated in 2006 in its Corruption Perception Index, where a higher number indicates higher level of corruption.

-- Ethiopia signed a double taxation treaty with, Algeria, Tunisia, and France in 2006 which made the total signed agreements about fifteen.

-- Ethiopia and Djibouti on November 18, 2006 signed a multi-modal transport agreement which enables the effective utilization of the port of Djibouti for the coming 20 years and a door-to-door cargo transit between the two countries.

-- A bilateral investment agreement was preliminarily signed between Ethiopia and Djibouti which allows citizens of both countries to invest in areas only restricted for domestic investors/nationals. This agreement does not cover areas of banking, insurance, micro-financing institutions, broadcasting and press. This agreement will be official after it is passed by the House of Peoples Representatives.

-- The nation's central bank, the National Bank of Ethiopia (NBE), has ordered that all bank processes concerning items being exported to China shall be undertaken and overseen by the Commercial Bank of Ethiopia (CBE) effective November 14,
¶2006.

-- A National Foreign Investment Promotion Advisory Council has been recently established with a view to conducting focused foreign investment promotion on textile and garment, leather and leather products, fruits and vegetables and agro-processing areas. Its two major tasks to collect organize and make available basic data with regard to land

allocation, utilities connection, investment opportunities, market and other relevant information. The next step is to track potential foreign inventors and convince them to invest in Ethiopia in the priority areas.
-- Ethiopian Telecommunications Corporation is about to embark on $1.5 billion expansion project through a vendor financing scheme signed with a Chinese company called ZTE.

The Government of the Federal Democratic Republic of Ethiopia (GFDRE) has publicly stated that the private sector will be an engine of development and that private capital should play an important role in the economy. To that end it has eliminated most of the discriminatory tax, credit and foreign trade treatment of the private sector, simplified administrative procedures, and established a clear and consistent set of rules regulating business activities. In 2003, Ethiopia formally applied for membership to the World Trade Organization (WTO) and a Memorandum of Foreign Trade Regime (MFTR) was submitted to the WTO Secretariat in January ¶2007. Though bureaucratic hurdles continue to affect implementation of projects, the Ethiopian Investment Agency (EIA), the main contact point for foreign investors, has improved its services and is now providing a highly expedited "one-stop shop" service that significantly cuts the time and cost of acquiring investment and business licenses.

In June 1996, the Ethiopian Government issued a revised Investment Code which provided incentives for development-related investments, reduced capital entry requirements for joint ventures and technical consultancy services, created incentives in the education and health sectors, permitted the duty-free entry of capital goods (except computers and vehicles), opened the real estate sector to expatriate investors, extended the losses carried

forward provision, cut the capital gains tax from 40 to 10 percent, and gave priority to investors in obtaining land for lease.

Amendments to Ethiopia's Investment Proclamation (Law) were issued in September 1998 and July 2002, further liberalizing the investment regime and removing most of the remaining restrictions. In the latest amendment, areas solely reserved for government investment were reduced to the transmission and supply of electricity through the Integrated National Grid System and postal services with the exception of courier services. Manufacturing of weapons and ammunitions and telecommunications services can only be undertaken as joint ventures with the government.

Ethiopia's revised investment code prohibits foreign firm participation in domestic banking, insurance and micro-credit services. Other areas of investment reserved for Ethiopian nationals include broadcasting, air transport services using aircraft with a seating capacity of more than 20 passengers and forwarding and shipping agency services. Professional service providers must be licensed by the Government to operate in Ethiopia. Also a foreign investor intending to buy an existing enterprise to operate it or buy shares in an existing enterprise needs to obtain prior approval from the Investment Agency.

In addition to those mentioned above, the amendment reserves the following areas of investments for domestic investors: retail trade and brokerage; wholesale trade (excluding supply of petroleum and its by-products as well as wholesale by foreign investors of their locally-produced products); import trade (excluding LPG, bitumen and upon approval from the Council of Ministers, material inputs for export products); export trade of raw coffee, chat, oilseeds, pulses, hides and skins bought from the market and live sheep, goats and cattle not raised or fattened by the investor; construction companies excluding those designated as grade 1; tanning of hides and skins up to crust level; hotels (excluding star-designated hotels), motels, pensions, tea rooms, coffee

shops, bars, night clubs and restaurants excluding international and specialized restaurants; travel agency, trade auxiliary and ticket selling services; car-hire, taxi-cabs transport services; commercial road transport and inland water transport services; bakery products and pastries for the domestic market; grinding mills; barber shops, beauty saloons, and provision of smith, workshop and tailoring services except by garment factories; building maintenance and repair and maintenance of vehicles; saw milling and timber making; custom clearance services; museums, and theaters and cinema hall operations; and printing industries.

Another important change made in the 2002 amendment has been the reduction in the minimum capital requirement of foreign investors from $500,000 to $100,000 per project for wholly foreign owned investments and from $300,000 to $60,000 for joint investments with domestic investors. The minimum capital required of foreign investors in the areas of engineering, architectural, accounting and auditing services; business and management consultancy services; and publishing is reduced from $100,000 to $50,000 for wholly foreign owned investment; and to $25,000 for joint ventures undertaken with domestic partners. A foreign investor reinvesting profits or dividends, or exporting at least 75 percent of the output will not be required to meet minimum capital requirements. The 27 percent equity requirement of local partners in joint ventures is also repealed.

The Ethiopian Government reviews investment proposals in a non-discriminatory manner. Foreign investors do not regard the screening process as an impediment to investment, a limit to competition, or a means of protecting domestic interests.

Most, but not all of the tenders issued by the Privatization and Public Enterprises Supervising Agency (PPESA) under Ethiopia's privatization program are open to foreign participation. In some instances the Government promotes joint ventures with Ethiopian private companies rather than outright sales. Some sectors are closed to foreign investment. Foreign firms participate through consultancy services preparatory to privatization, or through tendering on advertised privatization opportunities. Of the 360 public enterprises and branches pegged for privatization, 294 have been offered between 1994 and end of October 2006, 230 properties approximately worth $460 million have been sold; 18 returned to their original owners, while 10 retail shops and 1 state farm have been closed. These enterprises are mostly small enterprises in trade and other service sectors.

The privatization process is back on its track again. PPESA has put out a tender for 41 state enterprises in the past one year. Out of the 41 enterprises 20 are tendered for a partnership and outright sale. Among them are 9 food and beverage factories, 5 agro-industry and agriculture firms, and 6 transport and chemical enterprises

None of Ethiopia's utilities have been privatized to date, though the government is looking for foreign investor partners in selected telecommunications sectors. At the moment the Government has 91 state enterprises under its control.

There are no discriminatory or excessively onerous visas, residence, or work permit requirements regarding foreign investors. Foreign investors do not face unfavorable tax treatment, denial of licenses, discriminatory import or export policies, or inequitable tariff and non-tariff barriers. However, some Ethio-American investors who acquired privatized properties have experienced difficulties obtaining title deeds to the properties because of difficulties created by local level authorities. Some had problems acquiring land for investment purposes. Although federal officials have at times intervened to resolve these problems, a lasting solution requires policy level changes

CONVERSION AND TRANSFER POLICIES

-- Ethiopia's Investment Proclamation (Law) allows all foreign investors, whether or not they receive incentives, to freely remit profits and dividends, principal and interest on foreign loans, and fees related to technology transfer. Foreign investors may also remit proceeds from the sale or liquidation of assets, from the transfer of shares or of partial ownership of an enterprise, and funds required for debt service or other international payments. The right of expatriate employees to remit their salaries is granted in accordance with the foreign exchange regulations of the National Bank of Ethiopia. U.S. businesses represented in Ethiopia do not encounter difficulties in the repatriation of dividends.

-- The National Bank (NBE) retains a monopoly on all foreign currency transactions. The NBE supervises all payments or remittances made abroad. The local currency (birr) is not freely convertible. Ethiopia issued several proclamations (laws) in September 1998 that somewhat liberalized the country's foreign exchange market. NBE issued a directive in 2004 that allows non-resident Ethiopians and non-resident foreign nationals of Ethiopian origin to establish and operate foreign currency accounts. The minimum deposit is U.S. $100 and maximum $5,000. The Bank amended the directive in 2006 that the maximum amount to be deposited in a current account shall be $50,000. The directive also allows them to open a minimum of $5,000 in a fixed foreign currency account The Bank issued two other directives in 2006 regarding Flower Export and Foreign Exchange Repatriations and Provision for International Remittance Services. In general, firms complain that they are facing difficulty in obtaining needed foreign exchange at competitive rates.

-- In the last three years, the Birr has been fairly stable, undergoing a gradual depreciation from 8.57 birr per dollar in June 2004 to birr 8.75 per dollar in December 2006. Over this period, the differential between the inter-bank determined rate and the parallel (or "black market") exchange rate has been nearly narrowed significantly, though rates began to diverge in late 2005 due to speculations owing to domestic unrest and loss of investor confidence.

EXPROPRIATION AND COMPENSATION

-- Per Ethiopia's 1996 Investment Proclamation (Law) and subsequent amendments, no assets of a domestic investor or a foreign investor, enterprise or expansion may be nationalized wholly or partly, except when required by public interest and in compliance with the laws and payment of adequate compensation. Such assets may not be seized, impounded, or disposed of except under a court order.

-- No acts of expropriation have occurred under either the Transitional Government of Ethiopia (1991-95) or the Federal Democratic Republic of Ethiopia, which assumed power in mid-1995. Nevertheless, a few cases of U.S. citizens whose business properties were expropriated by the Marxist Derg government in power between 1974 and 1991 remain unresolved.

-- There is no right of private ownership of land. Land is leased from the state for up to 99 years. A few textile factories privatized in recent years were repossessed by the government because the new owners failed to pay debts owed to the government.

DISPUTE SETTLEMENT

-- According to the Investment Proclamation (Law), disputes

arising out of foreign investment that involve a foreign investor or the state may be settled by means agreeable to both parties. A dispute that cannot be settled amicably may be submitted to a competent Ethiopian court or to international arbitration within the framework of any bilateral or multilateral agreement to which the Government and the investor's state of origin are contracting parties.

-- Ethiopia's judicial system remains underdeveloped, poorly staffed and inexperienced, although efforts are underway to strengthen its capacity. While property and contractual rights are recognized and there are written commercial and bankruptcy laws, many judges lack understanding of commercial matters. There is no guarantee that the decision of an international arbitration body will be fully accepted and implemented by Ethiopian authorities. The Embassy routinely advises investors to specify that disputes will be settled by arbitration either in Ethiopia (the Chamber of Commerce now runs an arbitration center) or abroad due to the lack of experience of domestic courts.

-- Ethiopia is not a member of the International Center for the Settlement of Investment Disputes.

PERFORMANCE REQUIREMENTS AND INCENTIVES

-- The 2003 amendment to the Investment proclamation gives investment incentives for investors in specific areas.

-- Investors engaged in manufacturing, agro-industrial activities or the production of certain agricultural products and who export at least 50 percent of their products or supply at least 75 percent of their product to an exporter as production input are exempt from income tax for five years. An investor who exports less than 50 percent of his product or supplies his product only to the domestic market is income tax exempt for two years. Under special circumstances, the Board and the Council of Ministers could extend the tax exemption.

-- The government has also set up a special loan fund of $174 million through Development Bank of Ethiopia and made available land at low lease rates for priority export areas such as floriculture, leather goods, textiles and garments, agro-processing and related products. An investor can borrow up to 70 percent of the cost of the project from this special fund without collateral upon presenting a viable business plan and a 30% personal equity.

-- An investor who invests in the relatively under-developed regions of Gambella, Benshangul and Gumuz, South Omo, Afar and Somali will be eligible for an additional one-year income tax exemption. However, an investor who exports hides and skins after processing only up to crust level will not be entitled to the income tax incentive.

-- Investors who expand or upgrade existing enterprises and export at least 50 percent of their output or increase production by 25 percent are eligible for income tax exemption for two years.

-- Investors are allowed to import duty-free capital goods and construction materials necessary for the establishment of a new enterprise or for the expansion of an existing enterprise. Also spare parts worth 15 percent of the value of the capital good can be imported duty free. This privilege may be denied if the capital good and construction materials are locally produced and have competitive prices, quality and quantity.

RIGHT TO PRIVATE OWNERSHIP AND ESTABLISHMENT

-- Both foreign and domestic private entities have the right to establish, acquire, own and dispose of most forms of business enterprises.

-- State-owned enterprises have considerable de facto advantages over private firms, particularly in the realm of Ethiopia's regulatory and bureaucratic environment, including ease of access to credit and speedier customs clearance. Local businessmen as well as foreign investors complain of the lack of a level playing field when it comes to state-owned and party-owned businesses.

PROTECTION OF PROPERTY RIGHTS

-- Secured interests in property are protected and enforced, although all land ownership remains in the hands of the state.

-- One pending issue is the return of properties seized, "lawfully" or "unlawfully" during the Mengistu Haile-Mariam's regime (1974-91). The Government's position is that property seized "lawfully," that is, by court order or government proclamation published in the official gazette, remains the property of the state. The state may choose to sell such property if deemed appropriate. In most cases, property seized by oral order or other informal means is gradually being returned to lawful owners or their heirs through a lengthy judicial appeals process. Claimants are required to pay for any additions (buildings, generators, etc.) or improvements made by the Government.

-- Land for investment purpose is leased, with prices set by periodic auctions for urban land with established market floors. Land leasehold regulations, however, vary in form and practice by region. The June 1996 Investment Proclamation and subsequent amendments charge the Investment Authority with locating and facilitating the leasing of property by licensed investors.

-- Loan terms are generally quite short and very few mortgages are made. There is no system of recording security interests.

-- Also see section on Intellectual Property Rights.

TRANSPARENCY OF REGULATORY SYSTEM

Ethiopia's regulatory system is generally considered fair, though there are instances in which burdensome regulatory or licensing requirements have prevented the local sale of U.S. exports, particularly personal hygiene and health care products. Investment, business and other licenses for foreign investors can now be obtained from the Ethiopian Investment Agency in a matter of hours.

EFFICIENT CAPITAL MARKETS AND PORTFOLIO INVESTMENT
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-- Ethiopia does not have a securities market, although a private sector initiative to establish a mechanism for buying and selling company shares is under discussion.

-- While credit is available to investors on market terms, the 100 percent collateral requirement limits the ability of some investors to take advantage of business opportunities. Export oriented investors can borrow from the special fund at the Development Bank of Ethiopia without collateral for the amount up to 70 percent of the project cost.

-- Foreign banks are not permitted to operate in Ethiopia. Currently eleven banks; three state-owned and eight privately owned, are licensed to operate in the country. Some of the banks used to have extremely high non-performing loan (NPLs) portfolios. Due to their risk averse behavior and NBE's stringent supervision, currently the NPLs ratio is declining

and is below 20 percent. The state-owned Commercial Bank of Ethiopia has approximately two-third of the assets of the entire banking system.

-- The Ethiopian Government partially controls interest rates. NBE determines the floor bank deposit rate. Because there are no real securities markets, the Government cannot affect interest rates through market actions and retains the right to set interest rates. Loan interest rates are allowed to float. The minimum deposit interest rate is now 3 percent; adjusted downward from 6 percent in March 2002. Real interest rates remained negative in the past two years driven by the increase in the inflation rate. The Government argues this move was necessary to lower lending rates to encourage economic activity. The Government offers a limited number of 28 days, 3-month and 6-month Treasury bills, but prohibits

the interest rate from exceeding the savings deposit rate. In September 1998, Ethiopia reduced the minimum denomination of Treasury bills to about $600 (5,000 birr) in view of accommodating the private sector and individuals in the market. The yield on these T-bills is very low, 0.051 percent for 28 days, 0.048 percent for 91 days and 0.025 percent for 182-days bill in the first quarter of 2006/07.

-- There are no laws or regulations authorizing private firms to adopt articles of incorporation/association that limit or prohibit foreign investment, participation or control. There are no private sector or Government efforts to restrict foreign participation in industry standards setting consortia or organizations. There are no known instances of private firms attempting to restrict foreign investment, participation, or control of domestic enterprises.
-- There are no "cross-shareholding" or "stable shareholder" arrangements used by private firms to restrict foreign investment through mergers or acquisitions.

POLITICAL VIOLENCE

Ethiopia is relatively stable and secure for investors. Sporadic ethnic and religious violence in Oromia, Southern and Somali regions in recent years has not seriously affected foreign or domestic investors.

In fact the pace of both domestic and foreign investments particularly in Oromia has picked up in recent years. However, following the May 2005 elections, there was political unrest across the country and two incidents of demonstrations in Addis Ababa that turned violent, resulting in numerous arrests. Strikes, demonstrations, boycotts and shutdown of businesses by the government affected production, employment, trade, transport and other aspects of the national economy. By the year 2006, the unrest had largely subsided.

CORRUPTION

-- The UN Investment Guide to Ethiopia published in 2004 points out that, according to the private sector, routine bureaucratic corruption is virtually non-existent in Ethiopia. The guide adds that bureaucratic delays and difficulties certainly exist, but they are not devices by which officials strive to line their pockets.

-- Ethiopia ranked 114th out of 146 countries rated in 2004 (a higher number indicates a higher level of corruption), 137th out of 159 countries rated in 2005 and 130th out of 160 countries rated in 2006, suggesting a worsening corruption trend. There are suspicions that the frequent cancellation of telecommunications, power and other infrastructure tenders may be a result of corruption. In addition, state- and party- owned businesses receive preferential access to land leases and credit.

-- In May 2001, the Government launched an anti-corruption campaign in which a number of Ethiopian Government and private sector officials were detained. On May 24, 2001, the Government passed a proclamation on anti-corruption procedures and rules, and an Anti-Corruption Commission has been established. Since its establishment, the Commission has arrested many officials, including managers of the Privatization Agency, the state-owned Commercial Bank of Ethiopia, and private businessmen and charged them with corruption. There were no major arrests in the last two years.

-- It is a criminal offense to give or receive bribes, and bribes are not tax deductible. The Embassy has no knowledge of foreign investors ever being charged with corruption. The Ministry of Justice and the Anti-Corruption Commission are the Government entities with the primary responsibility to combat corruption.

BILATERAL INVESTMENT AGREEMENTS

To date, Ethiopia has bilateral investment agreements and treaties with China, Denmark, Italy, Kuwait, Malaysia, Netherlands, Russia, Sudan, Switzerland, Tunisia, Turkey Yemen, and recently with Djibouti. The Investment Agency has expressed interest in discussing a bilateral investment treaty with the United States. A Treaty of Amity and Economic Relations, which entered into force on October 8, 1953, governs economic and consular relations between the U.S. and Ethiopia. Ethiopia also has double taxation treaties with

Italy, Kuwait, Romania, Russia, Tunisia, Yemen, Israel and South Africa. There is no double taxation treaty between the U.S. and Ethiopia.

OPIC AND OTHER INVESTMENT INSURANCE PROGRAMS

The Overseas Private Investment Corporation (OPIC) offers risk insurance and loans to U.S. investors in Ethiopia. In October 2000, the then called Ethiopian Investment Authority (now Investment Agency) and OPIC signed an Investment Incentive Agreement and the agreement was ratified by the Ethiopian Parliament on April 8, 2003. OPIC provided political risk insurance in 1995 for a $48 million project by a U.S. firm to construct a sugar refinery. It also provided risk insurance to a U.S. firm involved in a road design project. OPIC also provided loan and risk insurance in 2003 for Med-Pharm project, a medical laboratory established by a U.S. company led by a U.S. citizen of Ethiopian origin. The project is now operational. Ethiopia is a member of the Multilateral Investment Guarantee Agency (MIGA).

LABOR

-- Ethiopia's labor force is estimated at 35 million, of which 85 percent are employed in subsistence agriculture, mostly as farmers. The Government and armed forces are the most important sectors of employment outside agriculture and provide work for almost 3 million people. The number of permanent and temporary workers employed in public sector manufacturing increased from 78,000 in 1978 to over 300,000 in 1999 and currently remains at about the same level. Approximately 40 percent of the urban workforce is unemployed. The high urban underemployment is partially offset by an informal economy.

-- Labor remains readily available and inexpensive in Ethiopia. Skilled manpower, however, is scarce in many fields.

-- Only about 300,000 workers are members of labor unions. Civil sector employees are not allowed to form unions. Most ILO Core Labor Standards have been enacted into law; the

Ethiopian Parliament ratified ILO Convention 182 on the Worst Forms of Child Labor in May 2003.

-- Child labor is not a pressing issue in the formal economy, but is common in rural agrarian areas and the informal economy in urban areas. Employers are statutorily prohibited from hiring youngsters under the age of 14. There are strict labor laws defining what sectors may hire "young workers," defined as workers aged 14 to 18, but these are not always enforced.

-- Ethiopia generally enjoys labor peace. There was no formal strike in 2005/06. The Government re-certified the Confederation of Ethiopian Trade Unions (CETU) in April 1997. Since its re-certification, CETU has focused on fundamental workers' concerns, such as job security; pay increases, severance pay, and health and retirement benefits. The right to form labor associations and to engage in collective bargaining is granted in the constitution. The new labor law that went into effect in February 2004 is generally considered pro-employer by labor unions. Workers who perform essential services are not permitted to strike.

-- Tri-partism emerged in May 1998 when the Government licensed the Ethiopian Employers' Association (EEA). The EEA is dedicated to maintaining labor peace and works in harmony with the ILO, CETU and the Ministry of Labor and Social Affairs. Its leadership supports the adoption of all ILO Core Labor Standards. In general, entrepreneurs believe that cooperating with labor is in their self-interest.

FOREIGN-TRADE ZONES/FREE PORTS

There are no areas designated as foreign trade zones and/or free ports in Ethiopia. Because of the 1998-2000 Ethio-Eritrean war, Ethiopian exports and imports through the Eritrean port of Assab are now prohibited. As a result, Ethiopia is conducting almost all of its trade through the port of Djibouti. Despite Ethiopia's efforts to clamp down on small-scale trade of contraband, unregulated exports of coffee, live animals, khat (a mildly narcotic amphetamine-like leaf), fruit and vegetables, and imports of cigarettes, alcohol, textiles, electronics and other consumer goods continues. The Government of Ethiopia provides support to exporters of textiles, leather and horticultural products,

including plots of land at low lease prices and a line of credit of $174 million (1.5 billion birr) to finance exports.

FOREIGN DIRECT INVESTMENT STATISTICS

-- Foreign direct investment in Ethiopia has gradually increased in the last few years. It increased from $40 million in 2002 to $70 million in 2004. Floriculture, horticulture in general, and leather are the sectors that have lately attracted FDI. Cumulated US capital inflow in the form of FDI to Ethiopia in the past 15 years has surpassed an estimated amount of $400 million. Current U.S. direct investment in Ethiopia is estimated at about $60 million.

-- U.S. companies with the significant presence and participation in Ethiopia's economy include Boeing, Cargill, Sheraton Hotels, Lucent Technologies, Cisco, Coca-Cola, Pepsi-Cola, Schaffer & Associates, Pioneer Hi-Bred Seeds, DHL International, Federal Express, United Parcel Service, Caterpillar, Mack Trucks, General Motors, Rank/Xerox Corporation, John Deere, Navistar and Hughes Network.
YAMAMOTO